

General Information Letter: Subtraction modification for income distributable to partners subject to Personal Property Tax Replacement Income Tax and election to pass-through to partners investment credit earned by partnership.

May 14, 1998

Dear:

This is in response to your letter to xxxx xxxxxx dated April 27, 1998, in which you request guidance from Legal Services. Department of Revenue ("Department") regulations require that the Department issue only two types of letter rulings, Private Letter Rulings ("PLRs") and General Information Letters ("GILs"). PLRs are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. GILs do not constitute statements of agency policy that apply, interpret or prescribe the tax laws and are not binding on the Department. For your general information we have enclosed a copy of 2 Ill. Adm. Code Part 1200 regarding rulings and other information issued by the Department.

Although you have not specifically requested either type of ruling, the nature of your question and the information provided require that we respond only with a GIL.

In your letter you have stated the following:

On April 15th, 1998, I called you in response to your letter to xxxxxxxx xxxxxxxx dated March 31 concerning the deduction of guaranteed payments on Form IL-1065. The letter I am referencing contained a notice that corrected an error in the Illinois Partnership Replacement Tax Return Instructions. My concern was the deduction of guaranteed payments as specified in the supporting worksheet for IL-1065, line 5d.

During our conversations, you indicated that you are not part of the technical staff and transferred me the taxpayer assistance department. In talking to the taxpayer assistance group about this notice, I do not feel that the issue was resolved.

I am writing to you asking that you forward this letter to someone in the legal department.

1) Inasmuch as we are increasing the deduction for income paid to partners subject to the replacement tax, doesn't it seem logical that we should be increasing the appropriate partner's taxable income from this partnership? When I asked taxpayer assistance, they acted as if there were no requirement to report anything to the partners, since it's not in the IL-1065 instructions.

2) On form IL-1065, Part 1, Line 2c, the instructions say 'Enter the amount from Form 1065, Line 10.' This amount is only the amount deducted on the trade or business. Why aren't guaranteed

payments deducted on Form 8825 or Schedule F also added back? And what about capitalized guaranteed payments? It seems to me that Form 1065, Schedule K, Line 5, would be a more reasonable number for Line 2c.

3) In regards to the new law enabling the partnership to pass the replacement tax investment credit to the partners, I have 3 questions.

A) Can the credit be split, that is, can the credit be taken partially on Form IL-1065 and the remainder passed to partners subject to replacement tax?

B) Form IL-477 instructions are silent as to what the partnership is supposed to do when the credit is passed to the partners. Are some of the numbers to be changed? This would affect a carryover computation and the amount carried to Form 1065, page 1.

C) Can a carryover be passed to the partners?

Ruling

Guaranteed Payments to Partners Subject to Replacement Tax

Section 203(d)(2)(I) of the Illinois Income Tax Act (the "IITA"; 35 ILCS 5/101 et seq.) allows a partnership, in computing its net income subject to Personal Property Tax Replacement Income Tax, to subtract:

An amount equal to all amounts of income distributable to an entity subject to the Personal Property Tax Replacement Income Tax.

The worksheet in the Form IL-1065 instructions which was the subject of the notice you received is used to compute the amount of this subtraction. Because guaranteed payments deducted by a partnership on Line 10 of the Form 1065 are already included in the partners' federal taxable income as income distributable from the partnership, they are properly subtracted under Section 203(d)(2)(I) if the partner is subject to Personal Property Tax Replacement Income Tax, and requiring the partners to add the guaranteed payments to their Illinois net income would double tax these amounts.

Also, the subtraction is allowed only for "income distributable" to a partner subject to Personal Property Tax Replacement Income Tax. The only guaranteed payments which are "income distributable" to partners are the payments shown on Line 10 of the Form 1065. Payments to partners for real estate which are, in fact, rents deductible on the Schedule 8825 are not distributions of partnership income, nor are capitalizable guaranteed payments, and these payments should not be subtracted under Section 203(d)(2)(I).

Pass-Through of Replacement Tax Investment Credit

Public Act 90-485 added Section 201(e)(9) to the IITA, providing that :

Each taxable year, a partnership may elect to pass through to its partners the credits to which the partnership is entitled under this subsection (e) for the taxable year. A partner may use the credit

allocated to him or her under this paragraph only against the tax imposed in subsections (c) and (d) of this Section. If the partnership makes that election, those credits shall be allocated among the partners in the partnership in accordance with the rules set forth in Section 704(b) of the Internal Revenue Code, and the rules promulgated under that Section, and the allocated amount of the credits shall be allowed to the partners for that taxable year. The partnership shall make this election on its Personal Property Tax Replacement Income Tax return for that taxable year. The election to pass through the credits shall be irrevocable.

This paragraph permits a partnership to elect to pass through "the credits" to which it is entitled under Section 201(e). There is nothing in this language which could be read to allow a partnership to elect to pass through to its partners some of the credits to which it is entitled, but not others. The requirement that the credit passed through must be allocated to "the partners" according to partnership shares precludes the partnership from electing to pass through credits only to partners who are subject to Personal Property Tax Replacement Income Tax.

The election applies to "the credits to which the partnership is entitled under this subsection (e) for the taxable year." Thus, the election applies to credits to which the partnership is entitled under Section 203(e) as a result of the carryforward of unused credits from earlier taxable years into the year for which the election is made.

Because the election covers all credits to which a taxpayer is entitled under Section 203(e) for a taxable year, including carryforwards from prior years, the partnership itself will be unable to take a credit under this section for a year for which it makes the election. Accordingly, in Part II, Line 8, of the Form IL-1065, a partnership making the election is instructed to enter "zero" on the line where this credit is actually taken. Even if the election is made, however, the partnership must still complete and attach the Form IL-477 in order to provide its partners and the Department with the information necessary for computing the credit allowable to each partner.

As stated above, this is a GIL which does not constitute a statement of policy that applies, interprets or prescribes the tax laws, and it is not binding on the Department. If you wish to obtain a PLR which will bind the Department with respect to the application of the law to specific facts, please submit a request conforming to the requirements of 2 Ill. Adm. Code Part 1200. Please note, however, that a PLR cannot apply the law to a hypothetical situation and a PLR is not binding with respect to a statement of facts which is incomplete or incorrect.

Sincerely,

Paul S. Caselton
Associate Chief Counsel -- Income Tax